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Message Text

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SUBJECT: HIGHLIGHTS OF BANK OF MEXICO'S 1977 REPORT

1. THIS CABLE SUMMARIZES THE INTRODUCTION OF THE BANK OF MEXICO'S ANNUAL REPORT FOR 1977, RELEASED FEBRUARY 22. REPORT FOCUSES ON DOMESTIC ECONOMIC DEVELOPMENTS IN THE PAST YEAR. BALANCE OF PAYMENTS AND OTHER KEY DATA REPORTED SEPARATELY.

2. IN A BRIEF DISCUSSION OF THE INTERNATIONAL SITUATION, THE REPORT NOTES A SLOWDOWN IN THE GROWTH OF WORLD TRADE AND THE GROWTH RATE OF OECD COUNTRIES. THE LACK OF DEMAND IS ATTRIBUTED TO LOWER RETURNS ON CAPITAL, UNUTILIZED INDUSTRIAL CAPACITY, AND INVESTOR CAUTION REFLECTING UNCERWVRMU'-5 43&-4$8,& 09)858:-) *-:594 , INTEREST RATES AND EXCHANGE RATES. REGARDING INTERNATIONAL CAPITAL MARKETS, THE REPORT NOTES THAT INDUSTRIAL COUNTRIES WERE LESS ACTIVE AND OPEC MEMBERS, DEVELOPING COUNTRIES AND SOCIALIST COUNTRIES INCREASED THEIR ACTIVITY. THE DEMAND FOR CREDITS REFLECTED THE NEED TO FINANCE TRADE DEFICITS AND TO REPLACE MATURING CREDITS THAT HAD BEEN PLACED IN LARGE AMOUNTS SINCE 1973, THE REPORT NOTES, ADDING THAT THE U.S.
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DEFICIT HAS CONTRIBUTED TO THE MORE RAPID GROWTH OF INTERNATIONAL LIQUIDITY.

3. ECONOMIC POLICY, THE REPORT NOTES, WAS GEARED AT RESTORING THE CONFIDENCE OF SAVERS AND INVESTORS, ASSISTING RECOVERY OF THE FINANCIAL SYSTEM, INCREASING TAX REVENUE AND UNDERTAKING PUBLIC SECTOR EXPENDITURES NECES-

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SARY TO MAINTAIN OVER THE MEDIUM AND LONG-TERM THE ECONOMY'S CAPACITY FOR EXPANSION.

4. THE REPORT NOTES LIMITED SUCCESS IN ATTAINING THESE OBJECTIVES. IT CITES THE REDUCTION IN HOLDINGS OF U.S. CURRENCY BY MEXICAN RESIDENTS, INCREASED TERM DEPOSITS IN THE BANKING SYSTEM AND OTHER MONETARY REFORMS. THE INCREASE IN GROSS DOMESTIC PRODUCT IS TENTATIVELY PUT AT 2.8 PERCENT, WITH THE INCREASE IN THE SECOND HALF CONSIDERABLY ABOVE THE FIRST HALF. THE IMPROVEMENT IN THE BALANCE OF PAYMENTS (DATA REPORTED SEPARATELY) IS ATTRIBUTED TO THE REDUCTION IN IMPORTS AND THE INCREASE IN COFFEE PRICES AND OIL EXPORTS. THE SERVICES BALANCE DID NOT IMPROVE BECAUSE OF THE DECLINE IN RECEIPTS FROM FRONTIER TRANSACTIONS. THE REPORT NOTES THAT WHILE THE BALANCE ON GOODS AND NON-FINANCIAL SERVICES WAS POSITIVE - $406 MILLION - INTEREST AND OTHER FINANCIAL PAYMENTS RESULTED IN A CURRENT ACCOUNT DEFICIT OF $1.8 BILLION. THE MONEY SUPPLY INCREASED 26 PERCENT FROM DECEMBER 76 TO DECEMBER 77. THE AVERAGE MONTHLY INCREASE OVER THE PERIOD 12 MONTHS EARLIER WAS 28 PERCENT, WELL BELOW THE INCREASE IN GDP IN CURRENT PESOS, NOTES THE REPORT, IN THE CONTEXT OF CALLING MONETARY POLICY ANTI-INFLATIONARY. THE REPORT DOES NOTE THAT EMPLOYMENT IN THE INDUSTRIAL SECTOR DECLINED IN 1977.

5. THE REPORT ATTRIBUTES THE POOR SHOWING OF PRIVATE IN-
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VESTMENT TO THE INCREASE IN PRICES OF IMPORTED CAPITAL GOODS, THE LIQUIDITY CRISIS CREATED BY THE DEVALUATION, THE DIFFICULTIES EXPERIENCED BY THE BANKING SYSTEM, AND THE DISRUPTION IN PLANNING OF NEW INVESTMENTS. THE REPORT NOTES THAT WHILE THERE WERE SIGNS OF INCREASED PRIVATE INVESTMENT IN THE LATTER PART OF 1977, THE RELATIVELY LOW LEVEL WILL IMPACT ON THE GROWTH RATE IN THE NEAR FUTURE. AS SIGNS OF RECOVERY, THE REPORT CITES (1) AN INCREASE IN CREDIT GRANTED THE PRIVATE SECTOR, (B) RECOVERY IN PRODUCTION IN THOSE INDUSTRIAL SECTORS ASSOCIATED WITH THE INVESTMENT PROCESS, AND (C) AN INCREASE IN IMPORTS OF CAPITAL GOODS. THE REPORT LABELS THE RECOVERY OF PRIVATE INVESTMENT AS "FRAGILE".

6. REGARDING 1978, THE REPORT STATES THAT IT IS POSSIBLE TO HOPE THAT THE CRISIS WHICH THE PRESENT ADMINISTRATION INHERITED MAY BE OVERCOME AND THAT THE COUNTRY MAY MOVE TOWARD THE ADOPTION OF THE BASIC OBJECTIVE OF A HIGH GROWTH RATE. TO ACCOMPLISH THIS, "IT WILL BE NECESSARY TO MAINTAIN A STRICT COORDINATION OF THE VARIOUS ECONOMIC POLICY ELEMENTS THAT WOULD MAKE POSSIBLE A REDUCTION IN INFLATIONARY PRESSURES IN ORDER THAT DOMESTIC PRICE IN-

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CREASES ARE COMPATIBLE WITH THOSE IN COUNTRIES WITH WHICH MEXICO TRADES". THE REPORT ALSO STATES THAT IT IS INDISPENSABLE TO INCREASE THE VOLUME OF PUBLIC AND PRIVATE INVESTMENT. THOMPSON

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